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C O N F I D E N T I A L SECTION 01 OF 02 REYKJAVIK 000131

SIPDIS

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SUBJECT: ICELAND ON ICESAVE: "WE ARE WILLING TO PAY"

Classified by: CDA Neil Klopfenstein for reasons 1.4 (b) and (d)

¶1. (C) SUMMARY: Multiple GOI sources privately expressed the government's intention to guarantee the Icesave deposits held by foreign depositors in the UK and the Netherlands. In addition, the Foreign Minister told the UK Ambassador that he expects the Althingi to approve the controversial guarantee agreement when it reconvenes next week. The UK Ambassador also reiterated that neither the UK, nor the Netherlands, is linking the Icesave issue to Iceland's EU accession. END SUMMARY.

Iceland intends to pay for Icesave

¶2. (C) An aide to former Foreign Minister Ingibjorg Solrun Gisladottir who is currently working behind the scenes for the Social Democratic Alliance approached CDA and stressed Iceland's intention to reimburse the losses of individuals who held Icesave accounts in the United Kingdom and the Netherlands. "We are willing to pay," she said. The aide explained that the current debate in the Althingi is about the specific terms of the loan, not about whether or not the depositors should be paid. If the terms of the loan can be agreed upon in the Foreign Affairs Committee, then the bill should pass.

¶3. (C) The UK Ambassador informed EmbOffs that he received the same information from the current Foreign Minister, Ossur Skarphedinsson, in a meeting Friday afternoon. Skarphedinsson explained that the current delay in the Althingi is not about whether to cover the deposits but rather over desired clarifications in the treaty. The two main sticking points, said Skarphedinsson, are clarifications that in the event of a default: 1) the British and Dutch governments will not take possession of Icelandic government-owned assets abroad and 2) Iceland's natural resources will not be used as collateral. The UK Ambassador told EmbOffs that the UK and the Dutch will not oppose such addendums. It is likely, according to the British Ambassador, that the two addendums will be added to the agreement next week when the Althingi reconvenes. Skarphedinsson said that he believes these additions will be sufficient to sway opinion on the bill and allow all sides to claim victory. It is Skarphedinsson's hope that the bill will pass as soon as next week.

¶4. (C) Yet another sticking point, however, may also be a clause in the agreement regarding Iceland's ability to renegotiate the terms should its debt burden exceed the amount in its depository insurance fund when Iceland must begin repaying the loan. (Note: Iceland will be given a seven year grace period before it must start repaying the loan. End note.) A member of the Civic Movement told EmbOff that the opposition parties believe this clause is too weak and must be strengthened.

¶5. (C) Skarphedinsson told the UK Ambassador that Prime Minister Johanna Sigurdardottir is losing patience with the delays and has told members of the Left Green Movement (LGM) within the ruling coalition to support the agreement by next Thursday or she will resign, causing the government to disband. This is a sizeable threat

that could hit home with several sitting members of the LGM who would be unlikely to be reelected to parliament in a new election. Skarphedinsson believes that the Prime Minister's ultimatum to the Left Green Party, in combination with the addendums, will provide the needed votes to pass the agreement by a narrow margin.

UK won't renegotiate Icesave agreement

¶6. (C) The UK Ambassador firmly stated that the UK will not renegotiate the Icesave agreement, despite calls from a small number of GOI officials to do so. From the UK's perspective, it holds all of the cards and is under no pressure to renegotiate the current settlement. It considers the Icesave loan to be like a mortgage agreement in which the borrower (Iceland) has no collateral and a poor credit rating, making it a more risky investment for the UK. In response to one critique that the interest rate on the loan is too high and that the UK and Netherlands are profiting from the arrangement, the UK Ambassador said that the GOUK is charging only what it is costing them to raise the money, plus administrative costs.

The LGM: Supporting Icesave to stay in power

¶7. (C) The LGM, the minority member of the ruling coalition, has lost significant political capital in voting to apply for EU membership and could lose more support by approving the Icesave agreement. The UK Ambassador posited that Steingrimur Sigfusson, Minister of Finance and head of the LGM, continues to support the ruling coalition's Social Democratic Alliance agenda because he realizes that this is the only way for his political party to remain in power. This is the only means the LGM has to continue to play a key role in building a new Iceland, one that replaces cronyism with transparency. In the

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meantime, the LGM can claim influence and victory based on the fact that the state has resumed a larger ownership role in key economic sectors than it had prior to the financial collapse, which is one of the LGM's main platform items.

Comment

¶8. (C) Despite conflicting reports in the media, the key players in the Icesave agreement, namely the GOI and the GOUK, are cautiously optimistic that the issue will be resolved in the next few weeks. Media coverage is beginning to reflect this shift through recent reporting that highlights the Icesave agreement as a decent deal compared to the other loans Iceland is receiving, including the IMF loan. All parties appear to agree that Iceland must guarantee the Icesave deposits for the minimum amount. While attempts have been made to link the recent EU accession talks to resolving the Icesave issue, the UK Ambassador and others have continued to reiterate the need to de-link the issues. Both sides believe that the two addendums covering the concerns of Icelandic assets abroad and use of natural resources should stifle the loudest detractors of the Icesave bill into supporting the ruling coalition government. If the Icesave bill is finally passed, it should be considered a resounding victory for the ruling coalition, as well as for the former Icesave account holders, paving a slightly smoother path towards restoring Iceland's international reputation.
KLOPFENSTEIN